14100

Executive Registry
77-5119

MEMORANDUM OF CONVERSATION

29 JUN 1977

Participants: United States

Secretary Blumenthal
Under Secretary Solomon
Samuel R. Gammon, Charge d'Affaires ad interim, Notetaker

France

Prime Minister Barre
Jacques de Larosiere, Director of the Treasury, Ministry of Finance
Francois Gavois, Assistant Director of the Cabinet

Time and place: 8:30 a.m., June 24, 1977
Matignon

Subject: Economic Problems

Distribution: Treasury: Solomon, Bergsten, Cross, Widman, Hufbauer, Syvrud, Ray, Hessler, Leddy, Schwartz; State: Cooper; Embassy Paris: Gammon, Dyche

THE AMERICAN ECONOMY

After an exchange of courtesies, the Prime Minister asked for Secretary Blumenthal's evaluation of how the American economy was doing. In reply, the Secretary said that our economy was doing reasonably well. It had been necessary to revise provisional estimates of this year's economic progress upward. The rest of the year looks quite good. He said that inflation figures are coming down, from a rather high first quarter, and the second quarter shows only 0.6% increase. The figure for the entire year should be about 7%, with the final quarter being at the rate of 6 1/2%.

In other fields of economic activity, the Secretary predicted that the U.S. economy would reach its target growth figure for the last quarter of this year of 5.8% in real terms. Consumer buying is increasing and investments are expanding also, but at a slower rate than the Secretary desires. On investment, he said we are somewhat behind what is needed, and he expressed some concern at the relatively slow rate of increase. For 1978 he foresaw real growth on the order of 5%. Consumer spending is already as high as is feasible; plant utilization is around 83% while unemployment is down to 6.9% last month, and he believes it will be about 6.5% by the end of the year, which will be somewhat ahead of target.

The chief problem on the investment front is business uncertainty over the President's energy program and what final form it will take. Tax reform is also an uncertainty factor but to a lesser extent, since most of the reforms are likely to be encouraging. The Secretary expressed the hope that the energy program would be enacted in the early Fall and that this would release the brake on investments.

BALANCE OF PAYMENTS

Turning to the balance of payments situation, the Secretary noted that both trade and current account balances are showing very large deficits. The current accounts deficit is about $12 billion. If this were only a one-time phenomenon it would be acceptable, but the Secretary expressed concern that continuance of the pattern in 1978 would put severe pressure on the U.S. Government. He noted that the trade accounts deficit of $25 billion is an all-time world record and heavy even for us.

Mr. Solomon noted that this situation would probably bring a weakening of the dollar and thus an enhancement of American export competitiveness. However, he said, it would be preferable if other countries increased their growth and their imports of American goods.

The Prime Minister expressed agreement with this sentiment. He warned that the U.S. should be careful in the trend on dollar exchange rates, noting that recent BIS comments showed some nervousness on this heading. On imports from the U.S., the Prime Minister regretted that France, owing to the cost of its oil imports, cannot increase its intake.

The Secretary agreed that the root cause of all countries' problems is the oil "tax". It is this which is causing inflation, unemployment, and political problems. Prime Minister Barre said that the oil "tax" was essentially a problem of transfers, but it differs from the problem of the 1920s and the immediate post-war era. Nevertheless, it inhibits any French effort to increase imports. Monsieur de Larosiere expressed somewhat greater confidence on the balance of payments issue. He believed that the U.S. must carry some of the load caused by oil import supercharges. Mr. Solomon in reply pointed out that it was difficult for the U.S. to carry this heavy load at a time when the Federal Republic and Japan were showing large surpluses on their balance of payments.

On balance of payments deficits, the Prime Minister took the view that the real question is psychological; if a deficit was tolerable psychologically, a country could carry it. Secretary Blumenthal said that even so $25 billion was too big for us. Monsieur de Larosiere summed up countries in surplus: Switzerland, 2 billion; Japan, 5 billion; FRG, 2 billion; Netherlands, 2 billion; OPEC, 40 billion.

Mr. Solomon pointed out that the U.S. is working on the Japanese Government on this problem, which is of overriding importance in our relations. However, Japanese officials have recently asked whether ending their balance of payments surplus or maintaining ceilings on their exports to us in certain areas takes priority. Mr. Solomon said he replied that they should increase their imports to bring about a balance of payments equalization. He added that the Japanese were inclined to confuse their priorities. He asked the Prime Minister's aid in influencing the Japanese. Secretary Blumenthal reinforced this point, stating that Japan must change its pattern of export-led growth.

Prime Minister Barre said that he always takes the opportunity of contact with Japanese officials to press them to end their trade barriers and to stimulate internal demand, pointing out to them that other countries also have oil import bills to pay. Japan must learn to balance its payments and not to squirrel away surpluses.

Secretary Blumenthal believes that responsible Japanese leaders understand this but they lack the political strength to change their system with its built-in export drives and to resist the pressures of Japanese business. The result is they tend to stall and avoid action, thereby hurting themselves in the long run. Mr. Solomon added that everytime the yen approaches the 2.70 exchange rate, the Government of Japan gets nervous and signals there will be no further appreciation. He expressed the view that Japan could better tolerate exchange rate changes than some other changes.

EUROPEAN ECONOMIES

Asked about the situation in Europe and in France, Prime Minister Barre explained in some detail the problem faced by Western European countries. In general, investment is slow, while requests to the Germans to be helpful on interest rates and by a more stimulative growth policy have not been complied with. The FRG has a serious deficit problem, particularly in the lending field.

For the U.K., the Prime Minister foresaw some slight improvement this year but found the situation there not very good. In Italy there is some improvement and perhaps the Italians might be able to pull off one of their combinaziones again.

In France, the unemployment problem is less serious than frequently judged, since nearly 1/2 the registered job seekers are women seeking an improved job or an ideal job rather than jobs frequently in idealistic or eleemosynary fields and this makes traditional employment-creating measures difficult. Mr. Solomon facetiously suggested that we set up a program to exchange our youthful unemployeds.

The Secretary asked about the French program for the government to pay initial employment social charges. Prime Minister Barre explained that this was for the first year of a new job. He also explained that the Government of France was subsidizing overseas employment for its citizens with French firms in order to overcome the traditional French reluctance to leave France.

The Prime Minister hailed his own successful efforts to control monetary supply. The expected budget deficit of 0.5% of the GNP is not serious. Most encouraging of all has been the first big deceleration in the rate of wage increases since 1969. The first quarter of last year showed a 4% wage increase while the first quarter of 1977 was down to only 2.3%. He hopes to be able to hold the overall increase for the year below 10%, which would mean a real-wage increase of only 1.3%.

The Prime Minister expressed gratification that the franc had been stabilized without the need for intervention. Asked whether this was not due to substantial borrowing abroad, he explained that the borrowing was for investment purposes and, therefore, essentially healthy. In any case, borrowing has dropped off slightly, and French reserves have also increased slightly. Returning to unemployment, he again said that it is primarily a psychological question as well as one with political impact. The true figure for French unemployment is probably around 650,000. He noted, however, that the figure in 1973 was only two-fifths as large. He noted also that unemployment had an inflationary impact.

Turning to the inflation question, the Prime Minister expressed regret that fruit and vegetable price increases at an annual rate of 20% (over the last four months) had damaged the fight against inflation. France had absorbed necessary utility price increases and price rises following the end of its brief price freeze and inflation would be at an 8.5% figure for the whole year. Without the fruits and vegetables impact, however, it would have been at only 7.8%. Nevertheless this compares very favorably with the 12% rate he found in September of last year on his entry into the Prime Ministership, so he feels he has really achieved a considerable success, without having to rely on the freeze. At 8 1/2%, France will be fairly close to the U.S. figures.

TRADE AND PROTECTIONISM

The Prime Minister next turned to the subject of trade and the protectionist threat. He explained France's recent imposition of textile quotas on eight products to last until the new multi-fibre agreement takes effect. He regretted this necessity, but it was politically essential to save the small textile producing communities in France, which had suffered an erosion of 100,000 jobs since 1974. Nevertheless, the Prime Minister emphasized, he personally is absolutely committed to the principle of free trade. It is also essential to fighting inflation. Indeed only four of the textile products have strict quotas imposed and they are primarily from the low wage countries like Hong Kong, Taiwan and South Korea. Milder controls are being imposed on the four other products which come from countries such as Morocco with favorable trade agreements with France or the EC.

Secretary Blumenthal asked whether the European Commission was not critical of France's unilateral action. The Prime Minister alluded humorously to his own long Commission experience and said that privately the Commission acknowledges the urgency of the French action and finds the measures basically sound, but must insist on the EC's right to be the authority to take such Article XIX actions. He said this is all right with France, if the Commission wants to in effect endorse French action in this manner. Replying to a question he expressed the view that other EC countries, such as Britain, would not seek to prevent this step or follow suit.

Secretary Blumenthal noted that without a system of requiring certifications of origin it would be hard to enforce the French quota against textile products imported through third countries inside the Community. The Prime Minister agreed that the controls may not in practice work very well, but he found that their psychological effect was in any event their principal value. Secretary Blumenthal pointed out that although the psychological effect was favorable in France, it had a negative impact in other countries. The Prime Minister agreed that such measures were unpleasant and reemphasized that he had limited them to the maximum extent possible.

Secretary Blumenthal described the heated discussions now going on in the U.S. over the multi-fibre agreement. Many Americans see it as a means of increasing the pressure for protectionism. He admitted that the U.S. had had recourse to controls on TV and shoe imports but had done this by bilateral discussions with South Korea and Japan. He referred the Prime Minister to the International Herald Tribune story this morning describing his and Ambassador Robert Strauss' efforts to avoid further protectionist measures. Such measures would inevitably be contagious. All countries, he urged, must be careful to avoid a spiraling cycle of protectionist measures.

The Prime Minister noted that this struggle was a daily battle for him in France. Monsieur de Larosiere added that he had been struck by the degree to which the opposition and the unions were tempted by the siren call of protectionism. Many leading Patronat figures were also tempted by "le vieux diable", protectionism.

Secretary Blumenthal advanced the idea we should find a psychological counterweight to offset the impact of the few small protectionist steps that were found to be unavoidable. He thought that if we could agree on a formula for multilateral trade negotiation progress, this would serve to generate hope and delay further little protectionist measures. He is urging Ambassador Strauss in his meeting with the EC Commission next month to seek agreement on a formula on how to proceed in the MTN negotiations.

The Prime Minister expressed the view that we must convince Europeans that a new formula for orderly trade patterns can be found; free trade is not a very good rallying cause with many Europeans. He agreed that if we could approach the problem under the guise of restructuring trade would ease protectionist pressures. He explained that he was not advocating market sharing arrangements. However something was needed to take care first of the problem of Japan, and the real risk of total Japanese dominance of some industrial sectors. He asked whether the Americans had seen the Japanese white paper for 1980-85, the projections of which clearly forecast Japanese dominance in many fields. The Secretary expressed interest in seeing this white paper. Mr. Solomon forecast Japanese concentration on microwave ovens next year and computers thereafter. de Larosiere interjected that cars and other forms of equipment were also Japanese priorities.

The Prime Minister then noted a second factor of the trade problem, which was those developing countries at the take-off point. These countries, and he cited Brazil, have absorbed Western know-how, credits and expertise, and now subsidize exports while limiting access to their growing domestic markets. This is intolerable, he said.

The Prime Minister criticized the system of generalized preferences which he complained had rewarded such take-off-point LDCs undeservedly. The Secretary noted that we are now debating just this issue with regard to tariff preferences, citing Venezuela as an example. Mr. Solomon expressed a differing view on generalized preferences. He found they helped bring certain successful LDCs into the system and wean them away from the Group of 77. It would be useful to win over Brazil and Mexico, for example. In any case, he pointed out that the generalized preferences had a duration of only 10 years.

EMERGENCY RELIEF MEASURES

The Prime Minister asked the Secretary's views on the Witteveen Facility and other relief plans. The Secretary responded that we hope on the Witteveen Facility shortly to have the Saudis final figure, which he hopes will be on the order of 2.5 billion SDRs. The Persian Gulf countries and other OPECs should then be able to bring it up to 5 billion, and he thought we might thus be able to create the Facility fairly soon. If we get the Witteveen Facility launched and the IMF quota subscriptions (seventh increase), the U.S. feels this will be enough for some time. Therefore, we believe it would be almost impossible to pilot a safety net contribution through the Congress unless the Witteveen Facility in the IMF first failed. In that event, with a major Presidential effort, Congress might come around. At present, however, the Administration has too many priorities in the Congress -- AID, Witteveen, IMF subscription -- to be able to tackle this at present. He is not very hopeful that the safety net will be forthcoming with U.S. participation and possibly it can never be created unless world conditions changed substantially.

The Prime Minister said France's policy is that it will not join the safety net without U.S. participation. Some countries, and he cited the Netherlands, have been suggesting a safety net without the U.S.

The Prime Minister noted the progress on aid to Portugal and the increase in the French contribution to $15 million.

Mr. Solomon asked whether the Government of France might not be able to separate out the sixth IMF quota subscription and the question of ratification of the IMF amended articles. To the surprise and pleasure of his staff, the Prime Minister proudly noted that he had wrapped up an agreement to approve the articles in the next Parliamentary session in his meeting with Gaullist leader Chirac three days ago. Chirac had listened to Barre's explanation and agreed to cooperate, but not in the present Parliamentary session. The articles would, therefore, be ratified early in the next session, around the middle of October. He did not encourage Mr. Solomon's hope that it would be possible to announce France's imminent ratification in the IMF meeting at the end of September. The Prime Minister stressed the sensitivity and secrecy of his agreement with Chirac, which could be torpedoed by prior publicity. Replying to a question, he said that Chirac does not understand monetary problems; Chirac has an internal political problem in his party with some of the old Gaullists who see the amendment of the articles as a U.S. triumph and therefore oppose it. However, the Prime Minister said he had explained this was not the case and had reminded Chirac that the latter had been Prime Minister in January 1976, when the amended articles were signed. The Prime Minister forecast that Chirac would lose very, very few of his RPR deputies on a vote on this issue.

Prepared by Samuel R. Gammon

Approve _____ABS_____ JUN 29 1977

Disapprove ______________

 CH

DEPARTMENT OF THE TREASURY

CLASSIFIED DOCUMENT ACCOUNTABILITY RECORD

remain affixed to document(s) transmitted herewith.

DATE RECEIVED	SUSPENSE DATE	LOG NO.

SECTION A — GENERAL

TO:	FROM:
The Honorable Stansfield Turner Director, Central Intelligence Agency Washington, D.C. 20505	Steven L. Skancke Room 3418, Executive Secretariat Main Treasury

CONTROL OR FILE NO.	CLASSIFI-CATION	DATE OF DOCUMENT	DESCRIPTION (*Identify Items such as Report, Letter, Memo, Etc. Unclassified Subject or Short Title, Copy Number and Number of Attachments*)	ORIGINATOR	NO. OF COPIES
14706	CONF	6/29/77	MemCon - Barre/Larosiere Meeting with Secretary Blumenthal	Gammon	1

SECTION B — INTERNAL ROUTING

TO	COPY NO.	DATE	PRINTED NAME	SIGNATURE
1.				
2.				
3.				
4.				
5.				

SECTION C — REPRODUCTION AUTHORITY

NO. OF COPIES REPRODUCED	AUTHORIZED BY (*Printed or typed name*)	SIGNATURE	DATE

SECTION D — DESTRUCTION CERTIFICATE

MATERIAL DESCRIBED HEREIN HAS BEEN (*Check appropriate block*):
☐ DESTROYED ☐ TORN AND PLACED IN A CLASSIFIED WASTE CONTAINER (*Burn bag*)

DESTRUCTION RECORD NO. | PAGE OR COPY NO.

PRINTED NAME OF CERTIFYING/DESTRUCTION OFFICIAL	SIGNATURE	DATE
PRINTED NAME OF WITNESSING OFFICIAL	**SIGNATURE**	**DATE**

SECTION E — TRACER ACTION

☐ SIGNED COPY OF RECEIPT FOR MATERIAL DESCRIBED ABOVE HAS NOT BEEN RECEIVED. PLEASE ACCOMPLISH APPROPRIATE SPACE IN SECTION F AND RETURN.

SECTION F — RECEIPT ACTION

☐ DOCUMENT(S) HAVE NOT BEEN RECEIVED ☐ RECEIPT OF DOCUMENT(S) ACKNOWLEDGED

25X1

(*Typed or printed name*) (*Signature*) 18 July 77 (*Date*)

REMARKS: Please return the original of this form to above address.

TREASURY FORM NO. 2747 (Rev. ADMIN. CIR. NO. 242 Aug. 1973)

Return Original to Sender

UNCLASSIFIED

EXECUTIVE SECRETARIAT

Routing Slip

TO:

		ACTION	INFO	DATE	INITIAL
1	DCI				
2	DDCI				
3	D/DCI/IC				
4	DDS&T				
5	DDI		✓		
6	DDA				
7	DDO				
8	D/DCI/NI		✓		
9	GC				
10	LC				
11	IG				
12	Compt				
13	D/Pers				
14	D/S				
15	DTR				
16	A/DCI/PA				
17	AO/DCI				
18	C/IPS				
19	DCI/SS				
20					
21					
22					

SUSPENSE ______________
Date

Remarks:

[redacted] 25X1

Executive Secretary

18 July
Date

3637 (5-77)

(EXECUTIVE REGISTRY FILE Treasury)